

FISCAL NOTE

Bill #: SB0019

Title: Revise taxation of new or expanded business enterprise property

Primary Sponsor: Jeff Mangan

Status: As Amended in Senate Committee

Sponsor signature

Date

David Ewer, Budget Director

Date

Fiscal Summary

**FY 2006
Difference**

**FY 2007
Difference**

Expenditures:

General Fund
State Special Revenue

Revenue:

General Fund
State Special Revenue- University System

Net Impact on General Fund Balance:

- | | |
|---|---|
| <input checked="" type="checkbox"/> Significant Local Gov. Impact | <input checked="" type="checkbox"/> Technical Concerns |
| <input type="checkbox"/> Included in the Executive Budget | <input checked="" type="checkbox"/> Significant Long-Term Impacts |
| <input type="checkbox"/> Dedicated Revenue Form Attached | <input type="checkbox"/> Needs to be included in HB 2 |

Fiscal Analysis

ASSUMPTIONS:

Department of Revenue

1. SB 19 creates two local option tax incentive programs for new or expanding business enterprises.
2. The first local option abatement programs would reduce the taxable value of certain property of expanding businesses by two-thirds (67%) for three years, and this abatement would apply to all mill levies including state mill levies. Under this first local option abatement program, qualifying new or expanding business enterprise property would include buildings, machinery, and fixtures used by the firm during the first three years of initial operation or following expansion.
3. The second local option abatement programs would reduce the taxable value of certain property of expanding businesses phased up equally over a 10-year period from 50% to 100%, and this abatement would only apply to local government (and school district) mill levies. Under this local option abatement program, along with buildings, machinery, and fixtures, a local government may choose to abate land and other types of property, such as gross proceeds.
4. The proposal removes the current definition of new industrial property and new industry found in 15-6-135, MCA, and repeals MCA sections 15-24-2401, 15-24-2402, 15-2404, and 15-24-2405; which apply to

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value-added manufacturing and expanding industry. SB 19 replaces these sections with a new definition for a new or expanding business enterprise and provides a similar tax incentive as the current law incentive in 15-24-1402, MCA, for local taxes.

5. The bill grandfathers industries currently receiving local tax incentives under 15-24-1401, MCA.
6. To qualify as a new or expanding business enterprise under the proposal, a firm must first meet certain criteria (Section 2). First, the firm must produce or plan to produce a value added product/commodity, or receive more than 50% of annual gross revenues from sales outside Montana. Second, the firm must add at least ten additional full-time employees in Montana and maintain the positions for three years. Third, employees must be paid the lesser of either the county average annual wage, or the Montana average annual wage as reported each year throughout the three-year qualifying period. Fourth, the tax incentive is only for the qualifying property that is necessary for the employment of the additional ten employees and the equipment it utilized throughout the three-year qualifying period.
7. The 2003 figure from the Department of Labor Quarterly Census of Employment & Wages shows the average annual wage paid in the private sector in Montana is \$25,657. Assuming an additional 16.5% of this salary for benefits, the minimum annual cost for hiring ten employees for purposes of this fiscal note is calculated as \$313,665 ($\$25,657 \times 1.165$ for benefits $\times 10$ permanent full-time positions).
8. Under current law, approximately 180 companies currently qualify for the new and expanding industry abatement program. The amount of taxable value associated with the current new and expanding industry property abatement program is provided in the following table:

Tax Year 2004		
Value of New and Expanding / New Industrial Properties		
Property Type	Tax Class	Tax Year 2004 Taxable Value
New Industrial Improvements	4	1,882,087
New and Expanding R & D Improvements	5	3,603
New & Expanding Ind- Air & H2O P C	5	3,965
New & Expanding Ind- Mach & Eq	8	3,166,810
3rd yr N & E Gas & Electric Pers	9	7,162
Centrally Assessed New & Exp Situs	9	58,374
Total		\$5,122,001

9. Under this proposal, these properties would continue to receive the current law abatement. However, any new applicants would have to meet the criteria under this proposal as summarized in assumptions #2 and #3.
10. Since the new qualifying criterion is different, the history of abatements to date cannot be used to project future impacts. There is no way to determine the number of new or expanding industries that would apply for these abatements. In addition, because the new abatement programs are local option programs, there is no way to determine how many applications would be granted or approved within such a process. Hence, there is no feasible way to project future impacts of this bill.

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11. The Department of Revenue anticipates no permanent, on-going administrative costs associated with this bill since there are no auditing or reporting requirements. However, the bill requires that once a local governing body has approved application for either of the abatement programs provided for in the bill, the application also must be approved by the Department of Revenue. In determining whether or not the new business will qualify for the abatement, the Department is to consider, among other things, the business enterprise's projected or contracted sales for that year, and *whether the abatement is necessary for the investment to occur*.
12. The bill further provides that the Department must charge a fee for the study of whether the business will qualify based on projected in-state and out-of-state sales, and on whether the abatement is necessary for the investment to occur. This study would be similar to contracted economic impact studies (EIS) undertaken to determine the overall feasibility of starting a business at a certain location, and would entail a substantial amount of professional econometric, statistical and other information-related resources. It is estimated that the fee for these studies would range from \$20,000 to \$30,000.

EFFECT ON COUNTY OR OTHER LOCAL REVENUES OR EXPENDITURES:

Local governments would see impacts to the extent to which they have new and expanding industry, grant the proposal's abatements, and have a certification from the Department of Revenue.

LONG-RANGE IMPACTS:

There is no way to determine the number of new or expanding industries that would apply for these abatements. In addition, because the new abatement programs are local option programs, there is no way to determine how many applications would be granted or approved within such a process. The general fund, and the university 6-mill account would be impacted depending on future new and expanding industries being granted the local option abatement program that includes state mill levies.

TECHNICAL NOTES:

1. The Title inserts 5-6-192, MCA into the list of statutes repealed. The correct reference should be 15-6-192, MCA. The proposal should be amended as such.
2. Under Section 2 (1), the firm must produce or plan to produce a value added product/commodity, or receive more than 50% of annual gross revenues from sales outside Montana **or** produce a value added product. However, other sections of this bill appear to require **both** a majority of revenue from sales outside the state **and** production of a value-added product. Section 1 indicates the incentives are for business enterprises "that produce goods or services then export those goods or services." Section 2 (6)(b), the language on qualifying employees says they must be necessary "to produce value-added products or commodities." Section 2(8) indicates value-added products do not include services except those incidental to the production of a product.
3. Section 2 (6)(a) requires employers to annually adjust wages for qualifying employees to the lessor of the state or county average annual wage as reported by the Department of Labor through the quarterly census of employment and wages program. It appears a firm could not choose to pay a higher amount under the current language of the bill.
4. Section 4(4) indicates that a local governing body may prescribe additional requirements a business enterprise must meet to receive the abatement. This authority does not extend to the state.

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5. Section 4 (6) provides the Department of Revenue authority to grant or deny the abatement only after the local government has approved the abatement for the local mills. Section 3 (3) states the abatement is for all mills levied. It should be clarified that all mills are abated if the application is approved by both the local governing body and by the state.
6. Section 4 (6) provides the Department of Revenue authority to grant or deny the abatement only after the local government has approved the abatement for the local mills. Would the Department of Revenue need specific reasoning to deny such an application? The bill does not provide any direction in this respect.
7. Typically, local option abatements only apply to local mill levies, and not state mill levies. The proposal allows local governments to abate state mill levies.
8. Section 6 (2)(c) says the local governing body may provide that real property “other than land, improvements or any combination thereof” is eligible for the tax benefit. However, under section 2 of the bill land was not included as eligible property.
9. The definition of “value-added” seems to include all aspects of business, including agriculture products. Under the proposal, very little business activity would *not* qualify under this definition.
10. The qualifying criteria specifies that the expanded property must be *necessary for the employment of the employees described, and the business must utilize the property throughout the qualifying period*. The terms necessary and utilize are vague, and could be called into question. Further definition of what qualifies as *necessary for the employment and utilized* would simplify administration of the bill.
11. The bill does not indicate an effective or applicability date. It is assumed the bill would take effect 10/1/2005, which does not provide sufficient time for implementation by the Department of Revenue.